



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Release Number: **201315031**

Release Date: 4/12/2013

Date: January 15, 2013

UIL: 4942.00-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Legends:

State	=
Ranch	=
Subsidiary 1	=
Subsidiary 2	=
Subsidiary 3	=
LLC	=
Retreat	=
Program	=
University 1	=
University 2	=
Year 1	=
Year 2	=
Year 3	=
Year 4	=

Dear

This is in reply to your ruling request dated June 15, 2009, along with supplemental information submitted on your behalf by your legal representative, regarding the consequences under §4942 of the Code of certain dealings with the property known as the Ranch.

Facts:

You are a Trust established in State to support certain religious organizations, and for general charitable purposes. The original Trust agreement required you to support certain beneficiaries, including University 1. At the time you were formed, §1.509(a)-4(i)(2)(iii) of the Regulations provided that a charitable organization described in §501(c)(3) of the Code could qualify as a public charity and as a supporting organization under §509(a)(3)(B)(iii) if it met the following three requirements: (a) it was a charitable trust under state law, (b) the supported organizations were beneficiaries of the trust, and (c) the supported organizations had the power to enforce the trust and compel an accounting. You originally qualified as a public charity on that basis. In 2006, §1241(c) of the Pension Protection Act invalidated §1.509(a)-4(i)(2)(iii). To qualify as a

Type III supporting organization, a trust must now meet the same requirements as a corporation, or any other entity, seeking exempt status under section 509(a)(3). You represent that the provisions of the original trust agreement did not meet the criteria necessary for you to continue to be treated as a supporting organization. Thus, your Trustees amended your Trust agreement in order to meet the statutory requirements applicable to a private foundation, and obtained the consent of the beneficiaries to the amendment. You further state that your Trustees obtained an Order Approving Petition for Confirmation and Approval of Conversion to Private Foundation Status from the Court having jurisdiction over you. You have represented that, effective July of Year 2, you have been a private foundation described in §§501(c)(3) and 509(a). Under the terms of the amended Trust Agreement, your assets continued to be held for the support of certain religious organizations and for general charitable purposes.

The Ranch property, located in State, was acquired over 20 years ago, in Year 1, to facilitate charitable programs for some of the original beneficiaries. At that time, you were the sole owner of Subsidiary 1. Subsidiary 1 was the sole owner of two other subsidiary corporations, Subsidiary 2 and Subsidiary 3. Subsidiary 2 owns a business enterprise which you represent to be excepted under the present holdings rules from an excess business holding. Subsidiary 3 was formed to hold the Ranch. You state that while held in this fashion, the Ranch was not held to any limitations as to use, and could have been used in a taxable manner. Following the amendment of your Trust Agreement and your conversion from a supporting organization to a private foundation, the Trustees restructured your holdings. Subsidiary 3 formed LLC, a limited liability company. In January of Year 3, Subsidiary 3 transferred all of its assets to LLC. In March of Year 3, Subsidiary 3 assigned its entire membership interest in LLC to you. You state that the transfer of the membership interest from LLC to you was treated as a liquidating distribution, and Subsidiary 3 recognized gain and paid income tax accordingly. You state that as of March of Year 3, you are the sole member of LLC, which holds the Ranch. LLC is a disregarded entity with respect to you and all of the Ranch's income and expenses are treated as direct income and expense items of you. Also, in March of Year 3, you adopted plans to hold the Ranch assets solely for use in carrying out your charitable retreat and sheep breeding activities.

The Ranch property includes a river, a farmstead, managed cropland, tame, wild, dry and river pastures, and fenced and unfenced range. You represent that all acreage suitable for cultivation of feed crops for sheep is currently producing crops, or is being improved using soil management techniques so that the acreage can be put into production. The fenced and unfenced range acreage is also in regular use, with sheep rotated among fenced-off sections, to assist in the collection of scientific research data. The Ranch also includes various structures related to sheep production.

You state that the Ranch is used to carry out two activities – the Retreat and the Program.

The Retreat began operations shortly after acquisition by Subsidiary 3, hosting clergy and providing room and board free of charge to visiting priests and nuns. The retreat season runs annually for six months. Retreat guests stay in the retreat center, and are prepared meals daily. You also pay for transportation to and from the Ranch for visiting clergy. The retreat amenities include a chapel, picnic facilities, access to many trails and recreational activities. The Retreat's Executive Advisory Committee, comprised of clergy leadership, general clergy and members of

the Ranch's local community, gives feedback on the retreat program and provides direction for alterations and improvements.

The Program involves a set of educational, research and development programs intended to enhance the quality, and increase the production, of range sheep in the western United States by developing and introducing into the market sheep with genetically desirable traits, and to further educational and scientific inquiry regarding sheep production. Prior to June of Year 4, the Program was operated in close cooperation with University 1. In June of Year 4, University 1 terminated its participation in the Program. In September of Year 4, the Ranch entered into an agreement with University 2 to continue the Program. The breeding program emphasizes genetic research and scientific development in conjunction with University 2. You represent that the results of the Program's research are made available to students for educational purposes, and more broadly to the public by way of publications in scientific and trade journals. You also conduct additional educational activities pertaining to sheep farming, both in conjunction with University 2 and otherwise.

As part of the Program, you sell breeding sheep to farmers, culled sheep to slaughterhouses, and wool. The breeding sheep are sold at auction. A primary purpose of such sales is to introduce the Ranch's genetically superior sheep into the marketplace, thereby improving the genetic quality of sheep in the United States generally, and for that reason you do not sell culled sheep for breeding purposes. Culled sheep are instead sold to slaughterhouses. You represent that you could sell culled sheep at higher prices to breeders, but that such sales would undermine your goal of increasing the genetic quality of sheep in the United States.

Expenses from operating the Ranch significantly outpace revenue from sales of sheep and wool. You represent that you operate at a significant loss because your focus is on furthering your charitable, educational and scientific goals, and not on realizing profits. You represent that, at least since March of Year 3, no portion of the Ranch is held for the production of income or for investment.

You represent that the entirety of the Ranch's acreage is used exclusively for either or both of the Retreat and the Program.

Ruling Requested:

The Ranch is used and held for use directly in carrying out your charitable, educational and scientific purposes within the meaning of §4942(e)(1).

Law:

Section 4942(a) imposes on private foundations (other than "operating foundations" as defined in §4942(j)(3)) an excise tax of thirty percent on a foundation's undistributed income.

Section 4942(c) defines the term "undistributed income" as the amount by which the private foundation's "distributable amount" exceeds its "qualifying distributions." The amount of income required to be distributed by a private foundation with respect to a particular taxable year is its "distributable amount."

Section 4942(d) defines the term "distributable amount" as any amount equal to (1) the sum of the "minimum investment return" increased by certain qualifying distributions recouped by an organization and reduced by (2) the sum of taxes imposed on the private foundation under subtitle A and §4940.

Section 4942(e)(1) defines the term "minimum investment return" as five percent of the excess of (A) the aggregate fair market value of all assets other than those which are used (or held for use) directly in carrying out the foundation's exempt purposes, over (B) the acquisition indebtedness (determined under §514(c)(1)) without regard to the taxable year in which the indebtedness occurred.

Section 53.4942(a)-2(c)(2)(v) excludes from the assets taken into account in determining the "minimum investment return" any asset used (or held for use) directly in carrying out the foundation's exempt purpose.

Section 53.4942(a)-2(c)(3)(i) provides, in pertinent part, that an asset is "used (or held for use) directly in carrying out the foundation's exempt purpose" only if the asset is actually used by the foundation in the carrying out of charitable, educational, or other similar purpose which gives rise to the exempt status of the foundation, or if the foundation owns the asset and establishes to the satisfaction of the Commissioner that its immediate use for such exempt purpose is not practical (based on the facts and circumstances of the particular case) and that definite plans exist to commence such use within a reasonable period of time. Consequently, assets which are held for the production of income or for investment are not being used (or held for use) directly in carrying out the foundation's exempt purpose.

Section 53.4942(a)-2(c)(3)(ii) provides examples of assets which are used (or held for use) directly in carrying out a foundation's exempt purpose. These may include real estate used by the foundation directly in its charitable, educational, or other similar exempt activities, any physical facilities used in such activities, such as research facilities and related equipment, and property leased by a foundation in carrying out its charitable, educational, or other similar exempt purpose at no cost or at a nominal rent to the lessee. In general, whether a particular asset is being held for the production of income or investment rather than used or held for use directly by the foundation in carrying out its exempt purpose is a question of fact.

Analysis:

Your purposes as stated in your governing instrument include support of certain religious organizations and other general charitable, scientific and educational purposes. You use the Ranch directly in carrying out these exempt purposes by supporting certain religious organizations through the Retreat, and by supporting the research and educational activities of University 2 (and, formerly, University 1). Although you sell sheep and wool, you operate at a significant loss because the purposes of the Program are to improve the quality of sheep production in the western United States and to enhance education and scientific research regarding sheep breeding, not to maximize profits. From the facts represented, it appears that the Ranch is not being held as an investment, but is being actively used to the maximum extent possible to carry out your exempt purposes.

Ruling:

Accordingly, based upon the foregoing and additional information provided, we rule that the Ranch is used and held for use directly in carrying out your charitable, educational and scientific purposes within the meaning of §4942(e)(1).

This ruling will be made available for public inspection under §6110 after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

This ruling is based on the facts as they were presented and on the understanding that there will be no material changes in these facts. This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described. Because it could help resolve questions concerning your federal income tax status, this ruling should be kept in your permanent records.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

In accordance with the Power of Attorney currently on file with the Internal Revenue Service, we are sending a copy of this letter to your authorized representative.

Sincerely,

Theodore R. Lieber
Manager, Exempt Organizations
Technical Group 3

Enclosure
Notice 437